HUNTON& WILLIAMS

CLIENT ALERT

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Contacts

If you have questions or would like more information, please contact any of the attorneys listed at the end of this Alert. Hunton & Williams' labor and employment law practice covers the entire spectrum of labor and employment litigation, arbitration, administrative practice before the NLRB, EEOC, and the DOL, federal contract compliance, wage-hour standards, workplace safety and health standards, workers' compensation, contractual rights and remedies, Sarbanes-Oxley and whistleblower claims, workplace investigations and client counseling under federal and state labor and employment laws.

Hunton & Williams LLP provides legal services to corporations, financial institutions, governments and individuals, as well as to a broad array of other entities. Since our establishment more than a century ago, Hunton & Williams has grown to more than 1,000 attorneys serving clients in 100 countries from 19 offices around the world. While our practice has a strong industry focus on energy, financial services and life sciences, the depth and breadth of our experience extends to more than 100 separate practice areas, including bankruptcy and creditors' rights, commercial litigation, corporate transactions and securities law, intellectual property, international and government relations, regulatory law, products liability, and privacy and information management.

The Whistleblower in Your Midst: Effectively Minimizing the Risks of the New Wave of Whistleblower Claims

Congress and financial institution regulatory agencies recently have placed whistleblower protection at the forefront of their agendas. In particular, both the Financial Industry Regulatory Authority ("FINRA") and the Securities and Exchange Commission ("SEC") have committed significant resources to whistleblower initiatives in recent months. Now more than ever it is critical for companies in the financial services industry to understand recent and anticipated legislative initiatives and to take steps to minimize the risk of exposure and liability in whistleblower claims. This is particularly true in the current economic environment, where allegations of financial mismanagement carry potentially sensitive public relations issues, have the potential for substantial fines and other non-monetary penalties, and are more likely to escalate into full-scale internal or regulatory investigations.

Congressional Whistleblower Protection Initiatives

In the wake of the current economic crisis, lawmakers are intent upon reforming the systems that led to the economy's collapse and view the whistleblower as an important component of those reforms. Just as we saw in the post-Enron regulatory initiatives, pending and recent legislation is designed to promote whistleblowing and protect the whistleblower.

Just last month, President Obama signed into law the Fraud Enforcement and Recovery Act ("FERA"). This legislation is intended to prevent financial fraud by, among other things, providing federal enforcement agencies with increased resources to ensure more comprehensive and effective whistleblower protections.

FERA is intended to strengthen the False Claims Act by extending whistleblower protections to government employees, third-party contractors and "tipsters" who report corporate wrongdoing or potential fraud to federal agencies. Under FERA, Congress authorized roughly half a billion dollars over the next two years to beef up manpower devoted to fraud detection and worker protection. These significant funds will be given to the U.S. Department of Justice, the FBI, the United States Attorney's Office and the SEC, among others.

FERA is not the only example of Washington's heightened interest in whistleblower protection. Indeed, one of the very first acts of the Obama administration, the American Recovery and Reinvestment Act of 2009, commonly known as the "Stimulus Bill," includes whistleblower

protections for employees who report what they believe to be, among other things, gross waste or mismanagement of stimulus funds. Given the vast reach of the over $700 billion in stimulus funds, these whistleblower protections will cut across industry lines and impact both small and large financial institutions in a way that other whistleblower laws do not. Moreover, because whistleblowing must relate to covered funds to be protected under the Stimulus Bill, coverage — i.e., whether a company received stimulus funds either directly or indirectly — likely will be a hotly contested issue. Importantly, these whistleblower protections allow for jury trials, do not include a statute of limitations, do not cap damages and cannot be waived as a part of any agreement, policy or condition of employment. Particularly noteworthy for financial services companies is that pre-dispute arbitration agreements, like those often used in the industry, will not be valid if they require arbitration of a dispute arising out of these whistleblower protections.

Congress will probably continue to expand whistleblower protection in the next few years. For example, Democratic Representative Lynn Woolsey has reintroduced and is committed to passing the Protecting America's Workers Act, which would extend whistleblower protections to employees who report, among other things, alleged violations of consumer protection laws.

Regulatory Whistleblower Protection Initiatives

Congress's efforts do not stand alone. In the wake of the Madoff scandal, the SEC has hired the Center for Enterprise Modernization, a government-funded research center, to analyze the SEC's method of evaluating and handling tips alleging securities law violations. Likewise, FINRA recently announced it has established the Office of the Whistleblower, through which individuals may report alleged illegal or unethical activity. This new office, headed by FINRA Senior Vice President Cameron Funkhouser, is intended to make the handling of "high-risk" tips more efficient and ensure that complaints falling under the jurisdiction of other agencies are properly referred to those agencies. This formal cross-sharing of information among governmental departments or agencies is a new development on the whistleblower landscape and puts both community owned banks, and small financial institutions at risk for such lawsuits just as it does the larger more public financial institutions.

The initiatives highlighted above put more arrows in the quivers of alleged whistleblowers and their lawyers. The increased attention by Congress and regulatory agencies, as well as the Democratic administration, also is likely to breathe new life into whistleblower claims under existing legal frameworks such as the False Claims Act and § 806 of the Sarbanes-Oxley Act, which prohibits publicly traded companies or officers, employees, contractors, subcontractors or agents of such companies from retaliating against employees who report, among other things, shareholder fraud. Although less than 2 percent of federal court lawsuits filed by alleged SOX whistleblowers have been adjudicated as having merit, employers should take little comfort in these numbers given the following:

- Plaintiffs and their lawyers undoubtedly will learn from these rulings and become more savvy about which claims to file and how such cases should be pursued.
- The number of layoffs in today's economic environment has deepened the pool of potential litigants.
- The Administrative Review Board ("ARB" or the "Board"), charged with issuing final agency decisions under the Sarbanes-Oxley Act, presently consists of two Bush administration appointees. With three vacant positions to be filled by Hilda Solis, the Obama administration's newly confirmed Secretary of Labor, the ideological balance of the ARB likely will be more receptive to claims previously viewed as lacking merit.
- Alleged shareholder fraud or harm to investors is at the heart of every Sarbanes-Oxley whistleblower claim. Indeed, Time magazine featured three prominent corporate whistleblowers as the collective "Person of the Year" shortly after the Sarbanes-Oxley Act became effective. The newsworthiness of such allegations has only increased since that time in the wake of the worldwide economic crisis.

The Future Of Whistleblower Claims

Based upon the changing political climate and the promise of tenacious whistleblower protection, whistleblower claims of every sort are expected to be at the forefront of litigation in the coming year. Unlike traditional retaliatory discharge claims, however, whistleblower complaints involving allegations of financial fraud and mismanagement, raise

unique and challenging issues that make comprehensive industry and operational knowledge imperative to navigating, defending and ultimately defeating non-meritorious whistleblower complaints.

These types of whistleblower complaints are more likely to escalate into full-scale internal or regulatory investigations of the allegations in the complaint made by the whistleblower. Employees who believe they have been retaliated against may also file a regulatory complaint with the SEC or seek the intervention of the United States Attorney's office to investigate the alleged wrongdoing, which can lead to invasive regulatory or law enforcement inquiries that may ultimately cost the company significant time and money to defend. In addition, allegations of financial mismanagement, particularly in the current economic environment, carry potentially sensitive public relations issues and the potential for substantial fines and other non-monetary penalties.

Given the high-profile and high-stakes nature of financial and regulatory whistleblower claims, they also are particularly attractive to a higher caliber of plaintiffs' lawyers. Based on our experience, we observe that the plaintiffs' lawyers who take these cases are more willing to invest their time, effort and resources in aggressively pursuing Sarbanes-Oxley and other whistleblower claims because they want to create a name for themselves in an emerging and potentially lucrative area of the law. These law firms are acutely aware of the economic pressure points that can be exerted in these matters and, regardless of a case's merit, this typically translates into an attempt to generate higher litigation costs, which calls for a well-planned and strategically executed defense.

Preparing For The Future

Hunton & Williams has extensive experience in defending financial services leaders against whistleblower claims and has a team of lawyers dedicated to monitoring related issues. The firm's experience brings with it the ability to examine business models critically, to develop individualized strategies for preventing whistleblower claims in the first instance, and to defend companies against those whistleblower claims that are filed. These strategies are integral to preparing for and protecting against the expected wave of whistleblower litigation.

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